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EDITORIAL DEPARTMENT NOTE

Industrial accountants have heard a great deal about accounting as a tool of control—so much, possibly, that some of us have come to feel that the use of accounting for control purposes is an attribute of industrial accounting not shared by what may be called general or financial accounting. But that such is not the case is well illustrated in the first article in the present Bulletin. Nowhere is control through accounts more essential than in the chain store field where widely scattered stores need to be knit together and controlled rather minutely if the organization is to operate as a unit. The present article gives a very clear picture of how this control is obtained in one chain store organization in connection with the important items of inventories, cost of sales and cash. The author of this article, Kenneth W. Thompson, received his formal education in a number of schools including Miami University, Columbia University and New York University. His varied business experience has included the position of Factory Accountant with the Riegel Paper Company of New York City, and the position of Chief Accountant for the Martin-Parry Corp. of York, Pa. For the past five and a half years Mr. Thompson has been connected with the Kroger Grocery and Baking Co., first as an accounting systems man, and for the past four years as Resident Controller of the Detroit Branch. A former member of the New York Chapter of N. A. C. A., Mr. Thompson is at present associated with the Detroit Chapter.

The second article in this Bulletin outlines a method of accounting for one division of one of Connecticut's most important industries—hat manufacture. The author's description of this industry will be found most interesting, and the solution which he presents for the special accounting problems of the industry will, no doubt, be found applicable in other fields. The author of this article, John H. Venman is a graduate of the Wharton School of Finance and Commerce of the University of Pennsylvania. Before entering college he served as an apprentice with the Atlas Furniture Company of Jamestown, N. Y. Following graduation in 1925, he was engaged as research man and later became a department manager with the Howland Dry Goods Company of Bridgeport, Conn. In 1931, Mr. Venman took charge of the selling activities of Lyon and Chase, a Bridgeport firm manufacturing accounting supplies, which led him into the public accounting field. In 1932 he established his own practice under the firm name of John H. Venman Co. During the past year Mr. Venman has been serving as Associate Director of Member Attendance for the Bridgeport Chapter.

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AUGUST 1, 1935

ACCOUNTING CONTROL IN A CHAIN OF 4,000 GROCERY STORES

By Kenneth W. Thompson, Resident Controller, Kroger Grocery and Baking Co., Detroit, Mich.

THE chain store idea had its inception more than a half century ago. The largest grocery chain in the world started in 1859 and, of course, at the present time is 76 years old. The company with which I am affiliated started in 1872 and is now 53 years old. So the chain store conception is no mere infant and, as it has progressed down through the years, its physical appearance and physical set-up has also improved.

Picture, if you please, in the days of the 90's or 1900's the era of the grocery store lighted with an oil lamp; heated with a tobacco splattered coal stove; bulk goods such as prunes, apricots, and beans displayed in open containers; crackers and sugar in barrels; the cheese also exposed to public eye, and the butter for public taste. Maybe also there was a cat sleeping behind the stove, or a dog, with a boy customer, stopping to scratch fleas besides that nice display of dried peaches—the next customer buying a combination of dried peaches and fleas. Contrast that with the modern store with its well lighted selling areas, clean in every detail; the clerk behind the counter wearing a fresh smock; with the displays including an attractive outlay of choice fruits and vegetables gathered from all corners of the country; yes, even delicacies from all over the world. Moreover, most of the goods are kept carefully covered to prevent contamination from contact with dust or individuals. From the ragged little unkempt urchin of its childhood, the chain grocery store has grown up to wear the striped trousers and spats of a respectable maturity. Instead of being merely a utilitarian dispensary of food stuffs, it has become a stylish shopping center, not less attractive than the department store.

And consider further the glamour of the chain store of today. The most important single item about the operation of chain stores is the personnel. Is it surprising to learn that the Atlantic and Pacific Tea Company has nearly 90,000 employees; that the Kroger Company employs 22,000 people? The store personnel—the sales

organization, if you please—furnishes the very life of the organization. But here we also find that the chain store provides a positive economic benefit to the employee. Stuart Chase in his book "Prosperity: Fact or Myth," written in 1929 and published in 1930, states that in a survey of 500 independent grocery store failures, it is found that 65% was due to inexperience, and 17% to fires, floods, sickness, and robberies. In other words, 82 out of every 100 small grocery merchants failing, did so because of lack of experience or lack of capital. A large chain today furnishes both experience and capital. The chain store experience is acquired through actual selling in the store and also through formal training schools. When a man is capable of being appointed as a manager he is given a store with $2,000 worth of merchandise, all the equipment necessary to conduct his business, the guidance, council, and support of some superior—some superintendent who calls on him at regular intervals to help him with his problems, coaching him over the pitfalls of ordering too much merchandise, guiding him in the disposal of perishable goods to avoid spoilage; in short, an expert is helping him run his business. Probably nine out of ten men who would fail as independent grocers can be saved as managers of chain stores. The man becoming a manager of a chain grocery store instead of courting failure can be saved and made an economic asset as a solid substantial wage earner in his community.

Consider the chains' progress in volume of business done. In 1922 it was estimated that 4% of the total retail sales in this country was handled by the chain stores; by 1930 that had grown to 21%. This volume of business was transacted in only 10% of the retail outlets. Especially impressive is the fact that the average grocery chain is happy if it can make a profit of only 2% of its sales. When you think of a chain store, you first think of the great national organizations like Woolworth's, Kresge's the Great Atlantic and Pacific Tea Company, or The Kroger Grocery and Baking Co. You think in terms of thousands of stores, for instance:

The Atlantic and Pacific has about	15,000
Woolworth's	2,500
Kresge	725
Kroger	4,300

But this is only part of the chain store business in the United States. It is stated fairly authoritatively that there are 7,000 local and sectional chain store organizations in addition to the big national chains that we hear most of. You can see, therefore, that the baby chain store of seventy-five or 100 years ago has grown to a vast idea and, accordingly, with it has grown a vast accounting field and numerous accounting problems.

Now, much of the accounting in any organization—be it a chain store, manufacturing plant, wholesale house, or department store—is similar to that in any other organization. By that I mean that in almost any business you will find a general ledger, effective accounts payable procedure, subsidiary ledgers, receivable and expense ledgers, equipment accounting in some form or other, budgets, and a cashier receiving and paying out company cash. Because these things are so universal and are basically so much alike in every business, I shall omit them tonight in this discussion of chain stores. There are certain things about chain store accounting, however, which are peculiar to that type of business and are not ordinarily found in other lines of business. Briefly, the most singular phases of grocery chain store accounting control are:

Inventory control
Computation of Cost of Sales
Cash Control

In this discussion we shall consider primarily these three major problems.

Inventory Control

The most elementary of these problems arises through inventory control and the accounting for merchandise inventories in each store location. In the retail chain grocery business, prices for a given area are usually determined by the headquarters office located within that area. Inventory control is developed through an application of the retail method. In other words, book inventories are maintained and physical inventories taken on a retail basis and any differences between book and physical inventories are stated in terms of retail values. Obviously, the control of inventories is very important in chain store operations in order to detect and quickly reflect excessive losses as a result of poor merchandise

handling on the part of store personnel, shop lifting, excessive and unaccounted for spoilage, or even actual stealing.

The arithmetic of inventory control in a grocery chain is as simple as 2 + 2 = 4. We said a moment ago that all computations are made on a retail basis. Merchandise is billed to the stores from the warehouse at retail values, hence, the opening inventory at retail, plus the purchases at retail, less sales at retail. leaves a balance which, of course, is the book inventory at retail. A physical inventory is taken at retail and the difference between the physical and the book inventories is the inventory discrepancy at retail. The following illustration will emphasize this idea a little more clearly, and to bring the matter down to cases, some hypothetical figures are inserted.

Opening Inventory at retail	$2,000
Purchases at retail	5,200
Total	$7,200
Less Sales at retail	5,000
Closing Book Inventory	$2,200
Physical Inventory	2,050
Shortage	$ 150 (3%)

In its utter simplicity, a store merchandise account is stated thus.

There are other factors, however, which enter into the computation of a book inventory. For instance, spoilage will occur. Inventory computation, therefore, should provide for spoilage. It is customary for the store manager, in his Weekly Merchandise Report, to state the amount of spoilage which has occurred in his store for that week. Accordingly, in accounting for store merchandise inventories, proper allowance is made for spoilage. One other important factor entering into an inventory computation is the effect of price changes. Prices are constantly fluctuating either in keeping with markets in general or to provide attractive bargains for special sales. Obviously, in our hypothetical case here, if a store manager has been instructed to sell Hershey Cocoa at 12½¢ instead of at the regular price of 14¢, or Bisquick at 30¢ instead of the regular price of 35¢ for a period of time, the proper allow-

ance must be made for the difference between the price at which the merchandise was actually sold on the special sale and the price at which it was billed to the store. Then, too, markets rise and it is necessary to increase the selling price of items on the shelves from time to time. Whenever this occurs, an additional charge must be made to the store inventory account.

Adjustment should be made for price changes and spoilage, and this is illustrated in the following case:

Opening Inventory at retail	$2,000
Purchases at retail	5,200
Total	$7,200
Add: Price Advances	50
	$7,250
Deduct: Price Declines	90
	$7,160
Deduct: Spoilage	100
	$7,060
Sales at retail	5,000
Book Inventory	$2,060
Physical Inventory	2,050
Difference	$ 10

The actual taking of a physical inventory is an interesting process. Inventories are taken by auditors who travel in crews of two—one of whom is a caller and counter and the other primarily a recorder. Upon entering a store, one auditor goes directly to the cash register and balances the store cash and, incidentally, takes off a cash register reading. Presently, they begin a count of the merchandise. They are not concerned with counts by commodities but only with counts by prices. They proceed down the shelves, one counting and calling and the other transcribing the counts on to a large sheet of columnar paper. The columns on this inventory sheet are marked for prices and as quantities are

called, entries are made in the proper price columns. The only words which pass between the auditors have to do with quantities and retail prices. For instance, if an item on the shelf is 15 bottles of 10¢ maraschino cherries, the caller says 15 at 10¢; the recorder enters 15 in the 10¢ column on the inventory sheet. The next item on the shelf happens to be a dozen bottles of 19¢ maraschino cherries, the called calls 12 at 19¢ and the recorder enters 12 in the 19¢ column. The auditors continue the count one item at a time, up and down the shelves, under the counters, on top of the counters, displays in the center of the floor, in the ice box, and finally the case lots in the storage space of the store. When the inventory is completed, it is forwarded to the office where it is extended and retail value computed. The value is then applied to the book value as determined in the foregoing illustration in order to arrive at the amount of inventory variation.

It is important to note that these inventories are not taken as one might suppose on the last day of the accounting period, but rather they are taken at all times during the month. A staff of men is employed to work daily at taking inventories and for each inventory taken, no matter whether it is on the first day of the period or the third, or the twelfth, or eighteenth or any other day, a cut-off is made on the books and the inventory difference determined. If the difference is reasonably close, say one-half of 1% of the sales, little consideration is given to it. If the difference should be excessive, however, either 2, 3, or 4% over or short, it becomes a matter of much concern. An excessive shortage indicates some unaccounted for loss; an excessive overage indicates an equally serious error either in record keeping or in store operation. Possibly you wonder how close to an even balance inventories can be maintained, handling as we do something like 1,500 items in hundreds of locations. Our record is one to be envied. In the year of 1934, our entire inventory adjustment for all locations, under our Detroit office, amounted to approximately $1.00 per store; in percentage it was actually only .003 of 1%.

Cost of Sales

Of course, a problem of wider scope and of greater importance is that of determining cost of sales in a grocery chain. For that matter, the very heart of any accounting system—be it for a

grocery, a factory, or a millinery shop—is its method for determining cost of sales. Basically, cost of sales in merchandising is determined by the old standard text book theory: Opening inventory, plus purchases, less closing inventory results in cost of goods sold. In the chain grocery business, it is customary to use a scheme known as the retail inventory method—a system employing the relationship between cost and selling prices to reduce the closing inventory from retail to cost. The method of reducing the closing inventory to cost is the only perplexing part of the problem. It was stated in the earlier part of this discussion that merchandise delivered from warehouses to stores is billed at retail values. This statement is only half the truth—actually, both retail and cost values are used in billing the stores and all store merchandise transactions are recorded at both retail and cost. The difference between retail and cost is known as the mark-up and the ratio of this difference to the retail value is known as the mark-up per centage. Notice, in particular, that in the retail business percentages are always stated on the selling price and not on the cost price. To reduce a retail closing inventory to cost, then, means merely to reduce it by the amount of mark-up as determined on a percentage basis for each particular store. Again the method for determining this mark-up can be brought out more clerly in an illustration:

	Retail	*Cost*
Opening Inventory	$1,000	$ 750
Purchases	4,000	3,050
Total Merchandise Available	$5,000	$3,800
Difference	$1,200 or 24%	

In this simple case it would be safe to say that the retail inventory at the end of the period should be reduced by 24% to arrive at the cost.

There are, however, certain other factors which enter into the cost of this merchandise. I refer particularly to price advances and price declines. These advances and declines, obviously, affect the total retail price of all the merchandise made available for sale in the store. Any advance or decline in retail values necessarily applies to the merchandise which was either in the inventory at

the beginning of the period or was delivered to the store during the period. Accordingly, the advances will be added to the total retail value of "Merchandise Available"; and the declines will likewise be deducted. In our assumed case above, then, let us add advances of $50 and deduct declines of $150. This makes a new total for "Merchandise Available" at retail of $4,900; the cost remains unchanged at $3,800. The difference, or mark-up, on all the merchandise available in the store is $1,100 and the mark-up percent is is 22.4%. This 22.4% then represents the ratio of mark-up in the retail value of the closing inventory.

The retail closing inventory is determined by subtracting from the net "Merchandise Available," the sales and known inventory losses, such as, spoilage and inventory shrinkage. To illustrate further, suppose that the sales of this store for the period in question amounted to $3,800; the spoilage to $50; and the inventory shrinkage to $10—all at retail. This constitutes a total relief, at retail, of $3,860, which, subtracted from the "Merchandise Available" of $4,900, leaves a closing inventory, at retail, of $1,040. The inventory, at retail, is then reduced by 22.4% or $233, and the closing inventory is finally computed at $807. The cost of sales then becomes:

Opening Inventory	$ 750
Purchases	3,050
Total	$3,800
Less: Closing Inventory	807
Cost of Sales	$2,993

Perhaps it will be stated that the use of percentages results in inaccuracies in the account. As a matter of fact, experience demonstrates that the errors by the use of percentages tend to offset each other inasmuch as a separate percentage is used for each store. The over-costing in one store tends to offset the under-costing in another store; consequently, the result is entirely satisfactory.

Some comment should be made with respect to costing meat sales. Here the problem is somewhat different. Until the present time, it has been felt impractical for obvious reasons to place a predetermined retail value on meat merchandise; consequently,

all transactions are handled on a cost basis. Closing inventory is determined by an actual item count and description of the merchandise on hand in each store at the end of the accounting period. Cost prices are applied, inventories are extended and totaled, and cost of sales determined directly therefrom.

The computation of cost of sales and closing inventory is only incidental to the preparation of a profit and loss statement and a balance sheet. Therefore, this whole proposition of costing of sales looks toward a much bigger problem of preparing the profit and loss statement for the entire company and, likewise, for the individual store. You may get some idea of the scope of our problem and the efficiency with which our accounting is handled when I tell you that a complete set of operating statements—balance sheet, profit and loss statement, and elaborate supporting schedules—is prepared for our company, comprising 4,300 grocery stores in 18 states, in about 7½ working days. Moreover, during the same 7½ days, we make up 4,300 individual store profit and loss statements.

Cash Control

None the less interesting in chain store accounting is the method of cash control. Let us follow for a moment the cash transactions of a store. When a sale is made the cash is rung up on the cash register, thereby starting a series of events having to do with the handling of cash. How may this cash be disposed of? Most of the cash finds its way into a bank through the armored car service. Some of it, of course, is reserved in the store and used for paying salaries and incidental store expenses; some of it is used, in relatively few cases, to purchase merchandise—mostly in country stores. At the end of an accounting period, when a cut-off is necessary, some cash is still on hand for deposit. A rather complicated accounting entry transpires with respect to handling of store cash and it may be set forth as follows:

Debit—Cash in Transit (for cash picked up by armored cars)
" —Store Expense
" —Store Merchandise
" —Cash on Hand for deposit
Credit—Sales
" —Cash on Hand for deposit (previous cut-off)

This transaction looks like a very simple method and, indeed, the problem becomes difficult only because of the number of stores involved. It is customary for each store to submit at the close of business each week a cash report on which is recorded cash register readings, deposits made, paid-outs for expenses or merchandise, cash carry over from the previous week, as well as cash carry over at the end of the current week. The cash from all sales must be accounted for either as deposits, paid-outs, or cash on hand. Spaces are provided in the cash report for recording each of these items. The reports from a group of stores are collected and placed on a peg board in such a way that the amount column is over-lapping on each report and immediately visible. A comptometer operator then proceeds to recap the individual lines for each of these items incidental to the cash reconciliation. When the recapitulate is completed, there has been established a reconciliation of all cash for all stores.

Especially interesting is the method of handling cash in a prominent chain. Armored car service is used to pick up cash in the store and prepare it for deposit in the bank. In each store there is a two compartment safe with a detachable dial. The dial on the door can be attached only by use of a key—one man in the store carrying the key and the other man knowing the combination; hence, two men are required to open the safe at any time. Within the safe are two compartments, one of which is accessible immediately upon opening the door and the other compartment is closed off by a second door, though there is an opening in the way of a slot through which envelopes containing money may be deposited in the second compartment. This slot is in such a position and so small that extractions cannot be made through it. The second, or inner, compartment is used for deposits and the outer compartment for storing change over night. As funds accumulate during the day, deposits are made up and placed in small envelopes, and slipped through the slot into the inner compartment of the safe. The door to that compartment requires two keys for entering, much the same as is required for the ordinary safety deposit box. One key is carried by the store manager and a second key is carried by the armored car attendant. When the armored car attendant arrives at the store, the outer door is opened, both keys are inserted in the inner door, and the inner door is removed;

thereupon, the deposit envelopes are withdrawn. The envelopes are then placed in a larger envelope, the armored car attendant picks up the deposit slip, signs a receipt for the number of envelopes which he has picked up, and he is on his way to transport the funds to the bank by way of the armored car office.

Possibly you think that the introduction of an outside agent to handle funds would result in serious losses. I have just completed a study of this situation covering a period of several months, during which nearly six million dollars was handled by the armored car company in more than 20,000 deposits. My study revealed that about 1,100 errors occurred, made up equally in number of overages and shortages. In other words, surprising as it may seem, 5 out of every 100 deposits made by store managers are in error. But still more surprising is the amount of money involved in these errors—shortages totaled $3,800 and overages, $4,800.

As a point of control, the cash register is highly significant. With its readings, of course, originates the credit to sales; from its reading comes the principal relief to store inventory for the inventory control which we discussed earlier; and, of course, it furnishes the first step in the control of cash receipts for the stores.

From this discussion, it is apparent that, after all, chain store accounting, while it does have some peculiarities, in its principal points of control, requires the keen accounting intelligence that a good cost accountant must have. The problems, while not of direct costing, are familiar to the cost accountant. In both factory and merchandise accounting is the control of cash significant, in both is it important to control inventories, and in both, of course, the determination of cost of sales is paramount.

ACCOUNTING FOR THE MANUFACTURE OF HATTER'S FUR

By John H. Venman, John H. Venman Co., Public Accountants, Bridgeport, Conn.

THE manufacture of felt hats is divided into three parts: the preparation of the fur that goes into the hat bodies, the manufacture of the hat bodies or "rough hats" as they are called in the trade, and finishing. Although this paper will deal only with accounting for the manufacture of hatter's fur, the first of the three divisions, it is none the less desirable to gain a summarized picture of the whole industry in order to understand the relationship of the first division to the other two.

Strictly speaking, a felt hat may be made of any material that will "felt," or interlace and mass together upon being shrunk. Two materials only are used at present, fur and wool. Over 90% of the felt hats produced in this country are made of fur felt, and for our purpose here we will confine ourselves to fur felt. The source of most of the fur that goes into our felt hats is the rabbit or hare skin. It is cheap and abundant, the animals grow fast and reproduce abundantly, and the fur is easily worked. The best skins are shipped into the United States from France and Canada; the greatest number come from Australia and New Zealand, and some are produced in the United States.

The skins are stripped from the animals without slitting, and the paws and tails are left adhering to the hide. They are cured and shipped flesh side out in bales weighing about 500 pounds. Most of the skins are imported through New York City by importers who specialize on that type of work, and the manufacturers and hatters buy from them as needed. The price of skins fluctuate violently, and oftentimes fortunes are made or lost on the rise or fall of the market.

Importance of Raw Material Cost

The comparatively large cost of fur in proportion to the value of the finished product (it averages around 40%) and the violent fluctuations in the raw material market give rise to certain peculiarities in the hatting industry. Very little raw material is stocked by the manufacturers of hatter's fur or "fur cutters" as they are

termed in the industry. The skins are usually bought to meet some specific order or demand, and not infrequently the manufacturer of the hat bodies will buy the skins and contract with a fur cutter to have them processed at a definite price per pound of finished fur. In such a case, the by-products—paws, tails, and the "pelt" or hide that is cut away from the fur is kept by the fur cutter as a part of his profits. The fur cutter, therefore, may have one lot of skins going through his factory on a contract basis side by side with another lot owned outright by himself. This situation must be kept in mind in outlining any accounting procedure for either the fur cutter or the rough hat shop.

Another effect of the raw material market on the hatting industry is that the goods are produced quickly as a rule, and only as the demand has shown itself. They are marketed promptly, and frequently notes and trade acceptances are taken to be used in financing production and raw materials. This is necessary not only to meet bills that are pending and avoid tying up too much capital in the business, but also in order to avoid any greater loss than is necessary from fluctuation either in market or in demand. As a result the industry may be working double shifts one month and the next month it may be shut down entirely.

Skins are usually bought in "lots," an arbitrary and convenient grouping of a certain number and quality. If a shipment is not treated as a lot, the skins are promptly sorted into lots when processing starts, and this lot follows through the entire history of the fur until it is sold to the rough hat manufacturers. The accounting system of the fur cutter, therefore, has to be built around the "lots" of skins.

Treatment of Skins.

The first step in the process of manufacturing hatter's fur is to open the bales of skins and dump them into drums of water in order to soften the hide and make it pliable. After they have become sufficiently soft and workable, the skins are taken out and slit down the belly by hand, and the paws and tails removed but carefully saved as a valuable by-product. The skins are then brushed by machine to straighten out the hair and fur, and the better and more expensive skins are then sent to the clipping and pulling department.

It is necessary here to explain the difference between "fur" and "hair." Hair is long and coarse and has no felting or interlacing qualities whatsoever. The "fur" is composed of tiny fibers that grow close to the skin and very thickly in winter. The fur keeps the animal warm, and the hair protects the fur. The fur cutter can use only the fur, and he must find ways and means of removing the hair from his product before it can be used in the manufacture of a hat. One of the means he uses for this is "pulling," using a device that catches the hair between two rollers and pulls it out without injuring the fur beneath it. Another device is "clipping," which uses an inverted lawn-mower sort of machine to clip the ends of the hair and depends on a later blowing operation in the rough hat shop to remove the balance. On the cheaper skins with shorter fur, clipping and pulling is entirely omitted, and the blowing operation is entirely responsible for the removal of the hair.

Both the better and the cheaper skins are now ready for "carrotting," a term used in the trade to designate the operation whereby nitrate of silver and certain other chemicals are brushed onto the fur in order to accentuate the twist of felting qualities of the fur. The wet skins are then spread out to dry, and after drying they are brushed again by machine.

Removing the Fur.

The fur is now ready to be cut from the skins. The skins are fed into a machine in which a series of sharp knives revolve very rapidly against the flesh side, and strip the hide from the fur. The shredded hide, or "pelt" as it is called, is saved as another valuable by-product of the plant, and the fur slides out on the other side of the machine onto a long wide table around which a group of girls are sitting. Each girl in turn takes the fur from what was and still looks like a skin, and carefully separates it into grades according to instructions, putting each part into a bag for that grade alone, which, when filled will weigh five pounds. The five-pound bag of finished fur is standard throughout the industry. The good fur, termed "cut fur," is now ready for delivery. Defective portions are separated by the girls and are reworked into "blown fur" in the cooking and blowing departments of the plant.

Treatment of By-Products.

The fur cutter usually sells his pelt for manufacture into glue. Some sell the other by-products—paws, tails and defective portions of the cut skins, but a great many manufacturers have facilities for salvaging and reworking these by-products themselves. This is done in a "cooking" department, and a chopping and blowing department. Those portions of the skin that have flesh or bone adhering to the fur and that are too small to go through the cutting machine are dropped into a large tub filled with sulphuric acid and other chemicals and kept hot with live steam. Here the flesh and bone are dissolved, but the hair and fur, being insoluble, float to the surface and are skimmed off. This is put through a drier and then sent to the blowers for final cleaning.

Other portions of the by-products of the plant, and the trimmings that are cut from the edges of hats being finished are put through a "chopper" in the blowing and chopping department. This disintegrates by physical means all the bodies falling into it, and allows the fine fibers of fur to become separated, from whence they can be taken to the blower and put into condition to be sold to the rough hat manufacturer.

Blowers are used both by fur cutters and rough hat manufacturers. This machine takes fur in which foreign matter is mixed, and by blowing the whole mass up through and again screens and revolving combs, causes the hair and dirt to fall so that it can be taken out, and causes the fur to rise so that it can be caught in another compartment where it can be packed into bags for delivery to the hat manufacturer. This grade of fur is termed "blown fur," and is of poorer quality and less expensive than "cut fur" because of its obvious mixed grades and broken and shortened fibers. Nevertheless it is an important part of a hatter's raw material, since it provides the "body" and "filling" to a felt hat at low cost, while the longer fibers of cut fur give the hat strength and shape.

The fur cutter's work is now completed. His finished product becomes the raw material from which the rough hat manufacturer makes hat bodies.

Manufacture of Rough Hats.

The rough hat manufacturer buys the various grades of fur necessary to make a certain kind of hat body. From the fur now

in his stockroom, he selects enough to make a "lot" of hats. This time the lot usually consists of that number of hats which a certain weight of fur, usually 100 pounds, will produce. Whatever the quantity of hats produced from this lot, it is kept separate and distinct until finished and sold, and any shortages must be accounted for by "defects" or "rejects."

The fur for a lot of hats is mixed in a hopper and then put through a blowing machine similar to those used by the fur cutter for a final cleaning. It is then taken to a girl who feeds the "former." She weighs out a certain amount of fur very carefully (about four ounces for a man's hat and usually less for a woman's) and this amount is drawn by suction into the former. The former is simply a large vacuum compartment in which a copper cone with perforated sides is placed over the only exit for the fur. The fur adheres evenly all around the cone, and the suction is turned off. Doors open into the compartment, and the cone is taken out and wrapped in a hot, wet piece of burlap. It is then dipped bodily into a tub of hot water, and left there for several minutes. This causes each fiber of fur to shrink and twist and interlock with its neighbors, or to "felt," as we call it. When the cone is removed from its hot water bath, the fur (now a long cone-shaped hat body) can be stripped off without separating.

The cone-shaped hat body now goes through various shrinking operations, consisting of wetting and kneading. It is then dyed, stiffened with glue and starch, stretched on a very clever machine with many fingers almost like those of a human being, and finally "pounced," or rubbed with sandpaper to cut off protruding fibers and give it a pleasing appearance.

This completes the work of the rough hat manufacturer, or "back shop." The hat bodies are now ready for the final processes by which they will be made ready for the consumer. This is done in the finishing shop, or "front shop," as the industry calls it.

The Finishing Shop.

In the finishing shop, the hat bodies are finished to the order of the customer. Size, color, hat bands, brim, shape must all be taken into consideration, and with the exception of certain sizes and colors, these details can be met by the finisher from the same lot

of hat bodies. The hat block forms the basis of his work, for each style and each size in that style must have its own set of blocks. The hat bodies are steamed to make them stretch, are pulled over the blocks, ironed by machine, trimmed on the edges or sewn as the style may demand, and then cleaned and polished with sand-paper. The linings, hat bands, size marks and ribbons are attached and the hats are then ready for shipment.

Most of the fur cutting establishments and rough hat shops are located in the towns and centers in which a skilled labor supply has been developed over a long period of time, such as Danbury and Norwalk, Connecticut. From convenience the two types of establishments are located near each other, but the third, the hat finisher, is usually located near his market, which ordinarily is the larger wholesale centers, such as New York or Chicago. While some firms care for all three divisions of the industry under their own roof and management, this is not always the case. A hat manufacturer will sometimes make and finish his own hat bodies, but the tendency in the trade seems to be toward the establishment of separately owned and managed units for each division.

From the foregoing a perspective of the entire felt hat industry may be obtained. It is now possible to return to the accounting problems of the fur cutter and to set up his accounting system in accordance with his needs and the requirements of the industry as a whole.

Departmentalizing the Plant.

The first step in solving the accounting problem of the fur cutter is to departmentalize his plant. While each individual will want his own plant departmentalized according to his needs and method of doing business, the following list of departments will serve to illustrate the principle to be followed:

A. Administrative and Selling.
B. Receiving.
C. Opening.
D. Clipping and Pulling.
E. Carrotting.
F. Cutting.
G. Cooking.

H. Blowing and Chopping.
I. Shipping.
J. Power, Light and Heat.
K. Plant Maintenance and Repair.

Use of Pre-Determined Unit Costs.

From our study of the processes of manufacture, it is quite evident that the raw material of a fur cutting plant flows through the factory in an established, routine manner. It therefore becomes necessary only to determine the costs of each department of the plant and the number of units produced in that department to control expenses and to record costs and inventory. It is not necessary to charge each lot with its detailed costs. If the costs are charged to each lot as it goes through a department on the basis of a carefully pre-determined cost per unit, the control of inventory and expense is easily possible, and yet the burden of record-keeping is greatly reduced. Furthermore, basing the cost of manufacture on an average figure spreads the costs of uneven production and other necessary but unforeseen expenses over the entire production for the period.

Chart of Accounts.

The next step, therefore, in our accounting program, is to lay out a schedule of accounts that will accurately reflect the financial condition of the company, its income and its cost of operations by departments. It is also necessary to set up accounts that will control inventory calculations and give us at the end of any period the values of materials, supplies, goods in process and finished goods on hand.

While the following schedule of accounts will be found to be far from complete, due to individual preferences and differences in size and equipment of each plant, it is nevertheless submitted as suggestive of the principles underlying the solution of this accounting problem:

1. Asset Accounts.
   11. Current Assets.
      110. Cash.
      111. Accounts Receivable.
      112. Notes and Trade Acceptances Receivable.
      113. Inventories.
   12. Fixed Assets.
      120. Buildings.
      121. Land.
      122. Machinery & Equipment.
         122A. Office Equipment.
         122B. Receiving Room Equipment, etc.
      123. Automobiles and Trucks.
      (Reserve for Depreciation Accounts may be designated by the symbol "R," thus 120R. Reserve for Depreciation on Buildings.)
   13. Prepaid Expenses.
   14. Other Assets. (Such as Goodwill.)
2. Liability Accounts.
   21. Current Liabilities.
      210. Accounts Payable.
      211. Notes Payable.
      212. Notes Receivable Discounted.
   22. Deferred Liabilities.
      220. Mortgages Payable.
      221. Bond Issues Payable.
      222. Deferred Accounts Payable.
   23. Personal Accounts. (Salary Accounts, etc.)
3. Capital Accounts.
   310. Capital Stock (if incorporated, otherwise the Capital Account of the Partner or Proprietor).
   320. Surplus.
   330. Undivided Profits.
4. Sales and Cost Control Accounts.
   41. Sales.
      410. Sales, Cut Fur.
      411. Sales, Pelt.
      412. Sales, By-Products.
      413. Sales, Blown Fur.

42. Purchases.
    420. Purchases, Skins.
    421. Purchases, Supplies.
43. Work in Process Accounts.
    430. Work in Process, Cut Fur.
    431. Cost Credit Accounts.
        431A. Cost Credit A/C—Adm. & Sell. Dept.
        431B. Cost Credit A/C—Receiving Dept., etc.
    432. Work in Process, Blown Fur.
44. Finished Goods Accounts.
    440. Finished Goods, Cut Fur.
    441. Finished Goods, Pelt.
    442. Finished Goods, By-Products.
    443. Finished Goods, Blown Fur.
45. Cost of Sales.
    450. Cost of Sales, Cut Fur.
    451. Cost of Sales, Blown Fur.
    452. Cost of Sales, Pelt.
    453. Cost of Sales, By-Products.

480. Discount and Allowances.

490. Discount on Purchases.

491. Interest Received.

492. Other Income (Specify).

5. Operating Expenses.
    51. Direct Expenses.
        510. Rent.
        511. Payroll.
        512. Outside Services.
        513. Commissions.
        514. Telephone.

    520. Supplies.

    53. Intangible Expenses.
        531. Insurance.
        532. Taxes.
        533. Depreciation.
        534. Medical Expense.

54. Apportioned Expenses.
    540. Power, Light and Heat.
    541. Maintenance and Repair.

Note: Each of the above operating expenses will be subdivided into departmental expenses, such as

    510A. Rent—Selling and Administrative Department.
    510B. Rent—Receiving Department.
    510C. Rent—Opening Department, etc.

Columnar Ledger Forms.

The forms shown as Exhibits 1 and 2 have been found very convenient in grouping department expenses and in eliminating a multiplicity of ledger pages. Exhibit 1 shows an expense ledger sheet, provided with a column for each department. Postings can be made to this form just as any other ledger account, and the various columns showing the departmental figures will show quickly and easily how each department shares in that expense. Exhibit 2 shows a departmental expense account subdivided by types of expense, making it possible to determine what the total expense of any department is and the items of which it is composed. Furthermore, the listing of one month or period under the preceding makes it possible to compare expenditures and locate any that are out of line.

Books of Accounts.

The books of account of a fur cutting establishment need not vary from those which are standard for any business: a purchase journal, sales journal, general journal, cash received and cash disbursed books, payroll book, general ledger, and the regular subsidiary accounts receivable and accounts payable ledgers controlled by the accounts receivable and accounts payable control account in the general ledger. The only modification needed is a wide ledger sheet to provide space so that any and all operating expenses may be subdivided by departments. These expenses should be analyzed before posting at the end of the month, so that only one posting from each book is necessary. It is our purpose here to show merely how the standard double-entry accounting system can be adapted to the peculiar problems of the fur cutter.

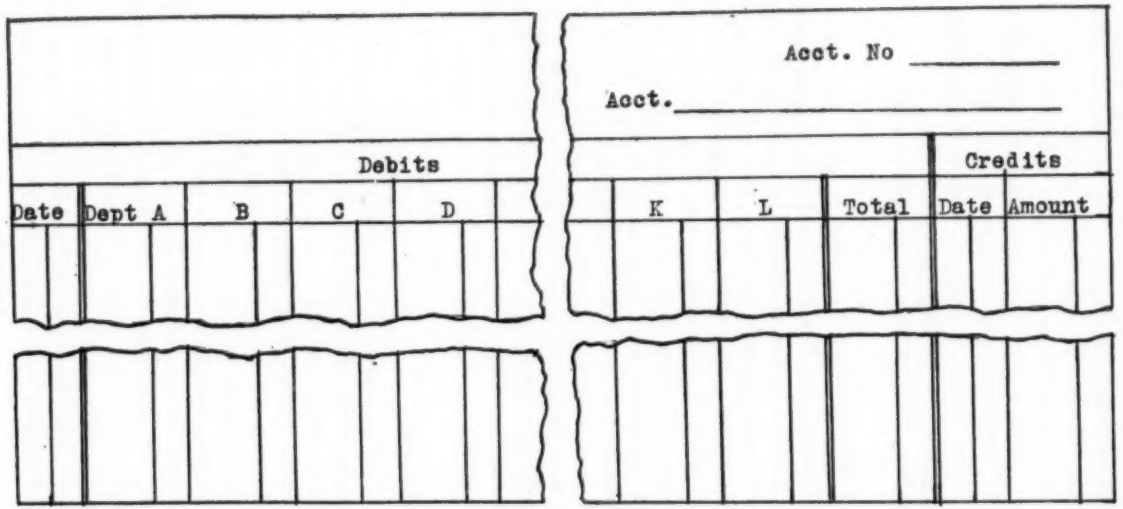


EXHIBIT 1
EXPENSE LEDGER SHEET SHOWING THE EXPENSE SUBDIVIDED BY DEPARTMENTS

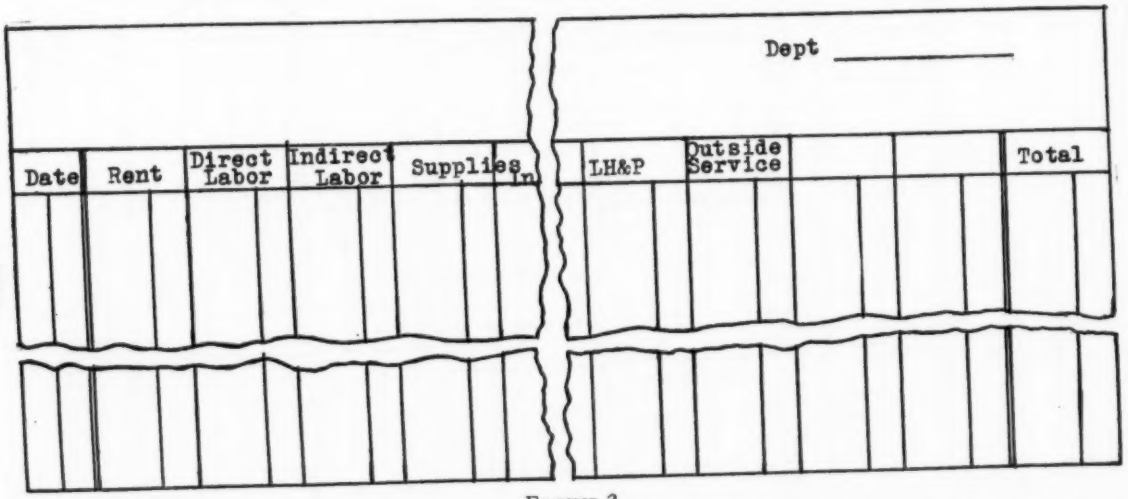
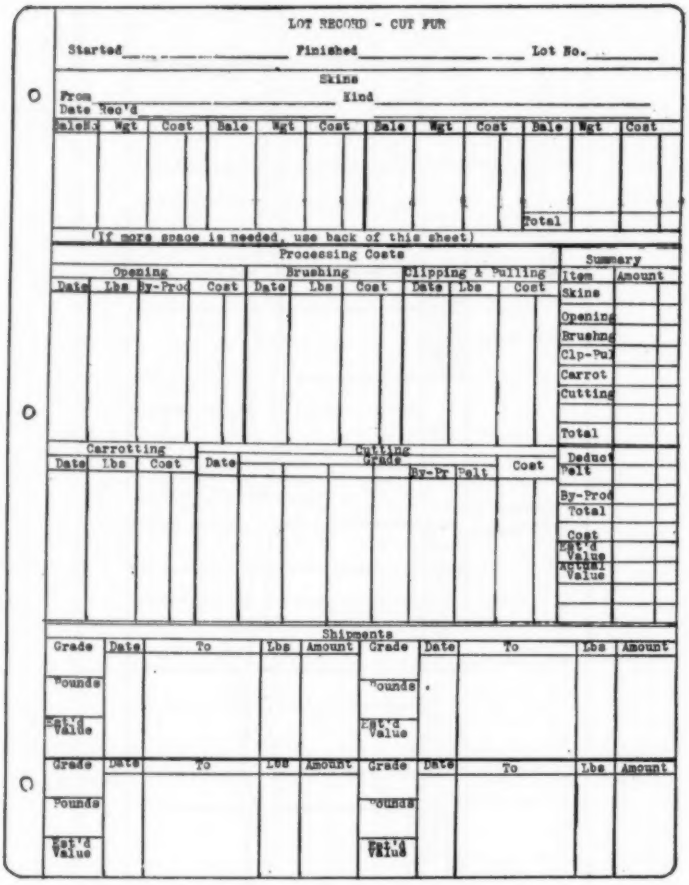


EXHIBIT 2
DEPARTMENTAL EXPENSE LEDGER SHEET FROM SUBSIDIARY LEDGER SHOWING TOTAL EXPENSE OF A DEPARTMENT



LOT RECORD - CUT FUR

Started _____ Finished _____ Lot No. _____

Skins

From _____ Kind _____

Date Rec'd _____

Bale No.	Wgt	Cost	Bale	Wgt	Cost	Bale	Wgt	Cost	Bale	Wgt	Cost
									Total		

(If more space is needed, use back of this sheet)

Processing Costs

Opening				Brushing			Clipping & Pulling		
Date	Lbs	By-Prod	Cost	Date	Lbs	Cost	Date	Lbs	Cost

Carrotting			Cutting					
Date	Lbs	Cost	Date	Grade		By-Pr	Pelt	Cost

Summary

Item	Amount
Skins	
Opening	
Brushng	
Clp-Pul	
Carrot	
Cutting	
Total	
Deduct Welt	
By-Prod	
Total Cost	
Est'd Value	
Actual Value	

Shipments

Grade	Date	To	Lbs	Amount	Grade	Date	To	Lbs	Amount
Pounds					Pounds				
Est'd Value					Est'd Value				
Grade	Date	To	Lbs	Amount	Grade	Date	To	Lbs	Amount
Pounds					Pounds				
Est'd Value					Est'd Value				

EXHIBIT 3

LOT RECORD—CUT FUR SHOWING COST OF PROCESSING AND DISPOSITION OF FINISHED CUT FUR

Basis for Applying Departmental Expense.

It is now necessary for us to decide what basis is to be used for distributing the expense of each department to the lots going through that department. From our observations in studying the processes of manufacture, it is evident that in the opening, clipping and pulling, and carrotting departments the basis should be the pound of skin processed. In the cutting, cooking, and blowing and chopping departments the basis changes to the pound of finished or partly finished fur. Of course there will be a divergence between the amount of expense actually incurred and that charged to Goods in Process, but by keeping careful account of number of pounds processed each day, as provided for in following forms, it is possible to gauge quite accurately the cost of each pound processed, and to change this cost as expenses rise or fall.

The basis of our accounting system is now complete. However, very important subsidiary records, such as the lot record and daily departmental reports are still to be mentioned. The best way of showing how they are related to the accounting system is to follow a transaction through from start to finish.

The Lot Record.

Skins are purchased, and recorded in the purchase journal under the account of Purchase-Skins. Next the factory manager gives orders that lot number 1 shall be processed, to consist of all the skins purchased. The factory order can be standard, so it is not illustrated. The factory superintendent requisitions the bales of skins to be used in lot number 1 from the storeroom, or, what is more likely to occur, when the shipment comes in, it is automatically called lot number 1. A lot record, such as the one illustrated in Exhibit 3, is prepared, and this form becomes the backbone of the cost and inventory record of the plant. All essential data concerning this particular lot of fur is entered on this sheet, and when completed it becomes a stock record until the fur leaves the plant.

The next event is that the plant incurs various expenses, among them being a payroll. All the operating expenses are charged not only to the proper expense account, but also to the proper departmental expense account, so that we may find out what it costs to run each department.

Daily Departmental Reports.

Now in order to know how far the work has progressed in each department and how much has been done on each lot, it is necessary to obtain from the department foremen daily reports of the work they have done. For that reason each departmental foreman reports daily the data required in order to complete the cost records. The forms, showing the information required are presented as Exhibits 4, 5, 6 and 7. These reports vary somewhat in accordance with the work of each department, but their purpose is the same, to inform the accounting department what has been done. With this information, we can keep our records complete.

The cost of the work done in each department is computed according to the set rate previously determined. The reports are then entered upon their various lot records. When a lot has been finished in any one department, all or nearly all the poundage of the original raw material should be accounted for, and if not, an investigation is in order.

Accumulation of Daily Reports.

In order to keep a running record of the value of work in process and of the value of inventories of raw materials and finished goods on hand, it is necessary to accumulate the information on the daily reports from each department. In other words a journal is kept for this information in all respects similar to a cash or purchase journal. The totals of the appropriate columns in this journal give us the information for the entries necessary to control our inventory and cost figures. The summary sheet, or cost journal need not be an elaborate book. In most cases a wide columnar pad similar to those used by auditors is adequate, and it can well be kept in neat penciled figures. Such a sheet with appropriate headings for the columns is set forth as Exhibit 8. The daily reports from the departments are entered on this sheet, one under the other, in the appropriate columns after being entered on the lot record. The by-products listed on the report of the opening department, and on the report of the cutting departments are charged at an arbitrary value daily under by-products goods. On the other hand, the by-products listed as being used by the cooking and blowing and chopping departments are entered at their arbitrary value in the by-product column of the section of the summary sheet

DAILY REPORT
COOKING DEPARTMENT

Date_____

Lbs Processed_____

Yield_____

Remarks

Signed

_____ Foreman

EXHIBIT 4

DAILY REPORT—COOKING DEPARTMENT

DAILY REPORT

Department_____

Date_____

Lot No.	Yield	By-Prod.

Remarks

Signed

_____ Foreman

EXHIBIT 5

DAILY REPORT—OPENING, BRUSHING, CLIPPING AND PULLING AND CARROTTING DEPARTMENTS

DAILY REPORT
CUTTING DEPARTMENT

Date_____ Lot No._____

Mach. No._____ No. in Crew_____

Started_____ Stopped_____

Pounds Processed _____

Yield

Grade	Pounds
Pelt	
By-Products	

Remarks

Signed _____
Foreman

EXHIBIT 6
DAILY REPORT—CUTTING DEPARTMENT

DAILY REPORT CHOPPING-BLOWING	
Date_____	
Materials Used	
By-Products	Cooked Fur
Yield	
Grade	Pounds
Remarks	
Signed _____ Foreman	

EXHIBIT 7
DAILY REPORT—CHOPPING AND BLOWING DEPARTMENT

Month Ending _____

Raw Materia		Charge - Work in Process								Charge Finished Goods						Coo	
		Opening		Clipping		Carrotting		Cutting		Cut Fur		Pelt		By-Prod		By-Pr	
Lbs	Amt	Lbs	Amt	Lbs	Amt	Lbs	Amt	Lbs	Amt	Los	Amt	Lbs	Amt	Lbs	Amt	Lbs	A

EXHIBIT 8
SUMMARY SHEET FOR JOURNAL ENTRIES

								Charge - Cost of Sales															
						Blowing																	
	King					By-P. Used		Yield		Cut Fur		Blown Fur		Pelt		By-Prod							
	od Used		Yield			Lbs	Amt	Lbs	Amt	Lbs	Amt	Lbs	Amt	Lbs	Amt	Lbs	Amt						
	mount	Lbs	Amt	Lbs	Amt																		

devoted to these particular departments. Similarly, if by-products are sold, the arbitrary cost of those sold is entered under the by-product column of the cost of sales section.

Work in Process Entries

At the end of the month or other period the columns on this summary sheet are totaled, and journal entries are made to record the summarized information on the books of the business.

The first entry records the cost of work in process, as follows.

Debit: Work in Process (#430)
  Credit: Purchases—Skins (#420)
  " : Cost Credit Account, Dept C (Opening) (#431C)
  " : " " " " D (Clipping) (#431D)
  " : " " " " E (Carrotting) (#431E)
  " : " " " " F (Cutting) (#431F)

The totals of the columns under the raw materials and the work in process sections are used for the above entry. A record should be kept of the number of pounds as well as the dollar value of the work processed. By comparing each month the total of the cost credits of each department with the total of the expenses for that department it is possible to see how nearly the expenses are being charged to costs. It should be kept in mind that a lean month must be balanced by a good month, so that changes in cost charged by each department on its production should not be made too hastily.

The next entry records finished goods. As each lot has been completed, the total value of the cut fur produced has been entered under its heading in the finished goods section of the summary sheet; the pelt produced by the cutting department has also been entered under its heading, as has also the by-products produced by the opening and cutting departments. These columns are totaled, and the following entry made:

Debit: Finished Goods, Cut Fur (#440)
  " " , Pelt (#441)
  " " , By-Products (#442)
  Credit: Work in Process (#430)

The next entries have to deal with the cooking and blowing departments. Both these departments may use part or all of the by-products of the plant independently of one another. Whatever they use is treated much the same as if it were sold to them, therefore the following entry is made:—

Debit: Work in Process—Blown Fur A/c (#432)
Credit: By-Products (#442)

It is necessary now to transfer the costs of processing in these two departments to Work in Process—Blown Fur Account. This done by a journal entry similar to those in the other departments:

Debit: Work in Process—Blown Fur A/c (#432)
Credit: Cost Credit Acct., Dept. G (Cooking) (#431G)
" : " " " , Dept. H (Blowing) (#431H)

Finished Goods

At the end of the period it is necessary to do one of two things in these departments in order to close out their Work in Process account to Finished Goods: either to cut off the supply of by-products until that on hand has been finished, which is by far the better way; or to take an inventory of the by-product on hand and credit that on this month's production and charge it the next month. Either way is correct, but for purposes of illustration here, we will assume that the first has been done. Therefore the following entry is in order:

Debit: Finished Goods—Blown Fur (#443)
Credit: Work in Process—Blown Fur A/c (#432)

We next come to the cost of sales section of the summary sheet. As each sale occurred, the cost of the goods shipped had been ascertained from the lot record and the blown fur record and entered on the cost of sales section of the summary sheet. At the end of the month, the various columns of this section are totaled, and the following entry is made:

Debit: Cost of Sales—Cut Fur (#450)
" : " " " —Blown Fur (#451)
" : " " " —Pelt (#452)
" : " " " —By-Products (#453)
Credit: Finished Goods—Cut Fur (#440)
" : " " —Blown Fur (#443)
" : " " —Pelt (#441)
" : " " —By-Products (#442)

Book Inventories Provided

It is now apparent that the Work in Process account has been charged with all the materials and expense connected with various lots in process of manufacture, and has been credited with all lots finished. The balance, therefore, is the value of the goods still remaining unfinished in the plant at the time the books are closed. Similarly, the balance in the Purchases—Skins account represents the value of the skins still remaining in the stockroom. The balance in the supplies account, as will be explained in the following paragraph, represents the value of supplies bought but unused. The balances in the Finished Goods accounts represent the value of the various items finished but still unsold and unshipped. It is therefore possible from these control accounts to make up a complete financial statement showing the condition of the company and the results of operations for the period. The one item that usually prevents the preparation of a financial statement for an interim period, the inventory, is automatically computed each period as a result of our cost data and journal entries.

Treatment of Miscellaneous Expenses.

It has been assumed that during the period of operation, any supplies withdrawn from storage for the use of any one department have been requisitioned, and these requisitions listed on a summary sheet similar to that shown in Exhibit 8. At the end of the month, these supplies are charged to the department, and credited to the general supplies account.

There are several departments whose expenses must be prorated and charged to the various producing departments of the plant. The expenses of the power, light and heat department and of the maintenance department must be apportioned equitably to

the other departments on the basis of use or production, and this expense will be taken into consideration in setting the cost of processing the skins.

No mention has been made of the costs of the receiving and shipping departments. These can best be apportioned to the work in process of manufacture by adding a certain amount to the cost of each pound of skin for receiving expenses, and by doing the same to each pound of fur sold to cover the shipping expenses.

Whether or not to charge administrative and selling expenses into the cost accounts of the plant is a moot question. It seems that the best practise is to leave it out of consideration in computing costs, inasmuch as the object of a cost system of this type is to find out and to know at all times what it costs to process the product that is going through the factory. Administrative and selling costs are not a part of manufacturing; they are a cost of doing business, and the difference between the gross profit on sales and the costs of doing business represents the net profit of the enterprise. By knowing the costs of manufacturing it is possible to know whether or not the plant is meeting its costs, its expenses, and whether or not it is showing a profit.

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In two sections—Section II

VOL. XVI, NO. 23 AUGUST 1, 1935

Applications for Membership

The Executive Committee has ruled that the names and addresses of all applicants for membership in the Association shall be published in the Bulletins for two weeks in advance of the date on which they are sent to the Director-in-Charge of Membership for approval. The following applications will be forwarded to the Director two weeks from the date of this Bulletin. Comments in regard to these applications which are received from members of the Association during this two weeks' period will be attached to the application before they are forwarded to the Director-in-Charge.

Baltimore

Smith, Winthrop Whitman, Mt. Vernon-Woodberry Mills, Inc., 506 Mercantile Trust Bldg., Baltimore, Md.

Birmingham

Schuett, Norman H., 2300 Fourth Ave. N., Birmingham, Ala. (Company Transfer)

Boston

Horie, Frank J., 29 Otis St., Boston, Mass.

Chicago

Skow, Carl C., 2120 Elston Ave., Chicago, Ill. (Company Transfer)

Detroit

Frehse, Arthur F., 1223 Penobscot Bldg., Detroit, Mich.

Milwaukee

Hanson, Arthur H., 2824 N. Summit Ave., Milwaukee, Wis.

New York

Lovell, Gordon Peck, 67 Myrtle Ave., Montclair, N. J.

San Francisco

Kimball, Robert E., Room 1002, 14 Montgomery St., San Francisco, Cal.

Outside Chapter Territory

Armstrong, William Victor, 62 Pitt St., Sydney, Australia.

BULLETINS PUBLISHED SINCE AUGUST, 1934

The Relationship Between Your Company Sales and General Business Activity	September 1, 1934
Controlling Distribution Costs	September 1
Management Under a Planned Economy	September 15
Accounting in the Paint Industry	September 15
Costs and Profits in Present-Day Accounting	October 1
Some Phases of T. V. A. Accounting	October 15
The Harris County Budget	October 15
The Depreciation Policy of the Bureau of Internal Revenue Under T. D. 4422	November 1
Treasury Decision 4422	November 1
Revamping Capital Structures	November 15
The Distribution of Holding Company Expenses Among Subsidiaries	November 15
Measuring Plant Capacity	December 1
Determining the Purchase Price of Cottonseed	December 15
Estimating the Special Order	December 15
Developing Costs at a Brush Factory	January 1, 1935
A Cost System for a Sparkling Ginger Ale Company	January 1
Hospital Accounting	January 15
Establishing a Control Over Hospital Income	January 15
Practical Standards—Their Development and Use	February 1
Practical Standards for Manufacturing Expense	February 1
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A Step-By Step Approach to the Determination of Profit at Varying Volumes	March 1
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Maintenance Costs and Control	March 15
The Modernization of Municipal Accounting	April 1
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A Method of Sales Analysis	May 15
Head Office Inventory Control	May 15
Inventory and Production Control for the Corset Industry	May 15
A Financial Budget for a Shoe Mfg. Co.	June 1
Accounting as Applied to the Baking Industry	June 15
Rubber Footwear Cost Accounting	July 1
The Costing of Rubber	July 1
The Gantt-Type Chart as an Aid in Budgetary Control	July 15
Accounting Control in a Chain of 4,000 Grocery Stores	August 1
Accounting for the Manufacture of Hatter's Fur	August 1